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IMPLICATIONS OF EU ENLARGEMENT

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TURKEY'S PERFORMANCE IN ATTRACTING FOREIGN DIRECT INVESTMENT: IMPLICATIONS OF EU ENLARGEMENT

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Abstract

This paper analyses Turkey's performance in attracting foreign direct investment (FDI). The paper is divided into three main sections. The first section analyses FDI in Turkey over time and relative to Central and Eastern Europe. The second section identifies the key factors determining investment location and on the basis of these factors assesses Turkey's competitive position. The third section examines the impact of EU enlargement on FDI in Turkey and explores whether the IMF agreement is sufficient for reducing obstacles to investment. The paper concludes that Turkey has under-performed in attracting FDI due to the slow pace of privatisation and political-institutional obstacles, of which chronic inflation is a manifestation. Structured interviews with global companies also highlighted lack of investment promotion as a major obstacle. While the IMF agreement will increase privatisation and reduce inflation, EU membership is vital if Turkey is to successfully compete for foreign investment.

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1. Introduction and Executive Summary

1.1. Introduction

Turkey is the largest economy in Eastern Europe, the Balkans, the Black Sea basin and the Middle East. It is the European Union's sixth biggest trading partner and the world's 7th largest emerging economy.

Yet foreign direct investment (FDI) flows into Turkey have rarely reached $1 billion in any one year - a fraction the level of FDI attracted to countries of comparable size and development like Argentina and Mexico and only one-quarter the level of FDI attracted into Poland.

A World Bank survey of multinational companies' perceptions of Central and Eastern Europe as a location for FDI concluded that: "For Turkey there is no easy explanation; we are left with the fact that investors speak more positively about it than the FDI inflows would suggest" (Michalet, 1997: 4-5).

Academic research to date also provides little explanation for the low levels of FDI flows into Turkey, or much analysis of FDI in Turkey in general. As Tatoglu and Glaister (2000: 5) state: "there is a paucity of information and study relating to FDI activity in Turkey."

Several international and private sector bodies have argued that Turkey must attract more FDI. The European Commission in its November 1999 progress report on Turkey highlighted the poor performance of Turkey in attracting inward investment as a barrier to economic development and integration. More outright, Inward Investment Europe argues that: "To end its current recessionary cycle Turkey needs significant foreign direct investment" (EUBIR, 2000).

The key objective of our study is to understand the extent of and reasons for Turkey's low level of inward FDI and to provide practical policy recommendations for increasing FDI in Turkey. This study hopes to fill a major gap in research relating to FDI in Turkey.

It is a critical time for more research on Turkey due to two fundamental events in Turkey's economic and political landscape. First, is Turkey's acceptance in December 1999 as a candidate member of the European Union (EU). Second, is the far-reaching $4 billion agreement with the International Monetary Fund (IMF). If successful, these events will dramatically change Turkey's investment climate. An important aspect of our study is therefore to examine the possible impact of these changes on future FDI in Turkey.

1.2. Executive summary†

In chapter two we evaluate Turkey's performance in attracting FDI both over time and relative to competitor locations. We find that FDI is playing a growing role in the Turkish

† Throughout the paper our main sources of primary research are data on FDI flows and projects and structured interviews conducted from April-June 2000 with senior executives in thirty leading multinational companies (MNCs) with investments in Turkey and global professional services firms who advise MNCs on investment location.

economy, in particular through new forms of investment, but that Turkey is under-performing relative to Central and East European Countries (CEECs) in attracting FDI. A key reason for Turkey's overall under-performance is the minimal level of privatisation-related FDI. In terms of mobile investment, Turkey has actually performed better than the CEECs as a whole. However, compared to Turkey's major competitors for investment we find that Turkey has greatly under-performed in attracting both privatisation and mobile FDI.

To understand why Turkey's has under-performed, in chapter three we review the existing literature to identify the key factors determining investment location, which we use to evaluate Turkey's competitive position for attracting FDI. We argue that the location of FDI reflects the match of corporate strategy with three major location determinants: economic; political-institutional; and enabling environment. We find significant evidence that Turkey has a very strong competitive position in relation to the economic determinants of investment location. Turkey is particularly well placed compared to competitor locations due to its economic size and dynamism and quality of its labour force.

We find, though, that in terms of the political-institutional determinants of FDI location, Turkey is in a much weaker competitive position. Political and economic instability, manifested as chronic inflation, and negative government attitudes towards foreign investors are major obstacles to FDI which are compounded by a weak enabling environment for privatisation-related FDI and a total lack of effective investment promotion.

In chapter four we explore the implications of the IMF agreement and EU enlargement for future FDI in Turkey. We find that the IMF agreement and EU candidate status are vital pre-conditions rather than advantages for attracting FDI into Turkey. Turkey will still face many challenges to increasing FDI. In particular, competition for FDI is intensifying and we argue that Turkey will face the erosion in its competitive position as a location for FDI when the CEECs join the EU before Turkey. In our policy recommendations for increasing FDI we argue that a vital pre-condition for Turkey to attract greater FDI is greater political and economic stability in order to reduce inflation and make progress in privatisation.

Turkey also needs to meet the requirements to join the EU, and we propose that Turkey could join the Single European Market before it joins the EU, as this would remove many obstacles to FDI. This argument also applies to other candidate countries that do not join the EU in the first wave. Hungary, the Czech Republic, and Poland are already attracting the major share of FDI in the region and the prospect of their joining the EU first will further widen economic disparities. We therefore recommend that the EU facilitates the enlargement process as quickly as possible for Turkey and the CEECs

We also strongly recommend that a new investment promotion strategy is needed for Turkey to develop its image, brand awareness, and provide much needed information to investors at the national and regional levels.

2. Turkey's Foreign Direct Investment Performance

2.1. Introduction

The key objective of this chapter is to analyse Turkey's performance in attracting FDI both over time and relative to other countries. We are careful to compare Turkey with countries that are actually competing for the same investment and we control for the different economic size of countries to gain a more realistic measure of performance. We also counter some of the limitations of traditional balance of payments FDI statistics by separating out the role of privatisation in FDI flows and through using project-by-project FDI data.

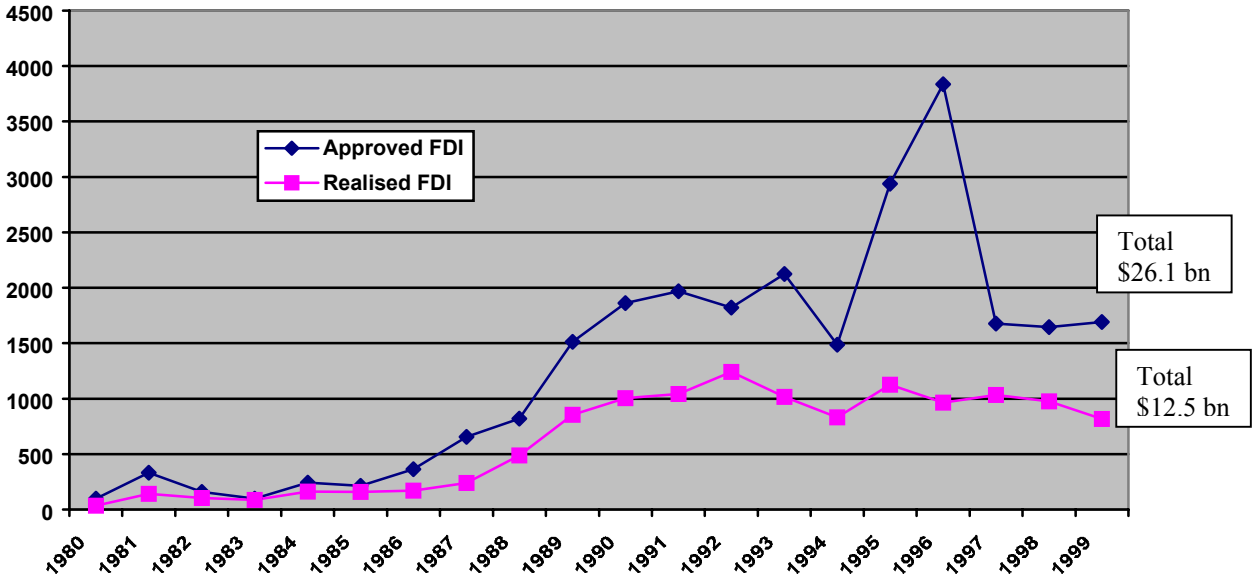
2.2. Turkey's FDI performance over time

The stock of FDI in Turkey was only $300 million in 1971, and up until 1980 the average annual inflow of FDI was only $90 million. As Balasubramanyam (1996) shows, this was far less than other comparable countries, and FDI did not increase significantly for most of the 1980s. It was only with a shift in Turkey from a protectionist trade regime to export-oriented economic liberalisation in the mid-1980s that FDI increased significantly.‡

As Figure 1 shows, annual FDI flows in Turkey grew rapidly from the mid-1980s, reaching $1 billion in 1990. However, FDI flows per annum have not increased for the decade since then. In other words, during the 1990s when global FDI flows accelerated – exceeding the growth in world trade since 1989 – FDI in Turkey remained static. An interesting observation in Figure 1 is the difference between approved and realised FDI. Approved investment indicates what investors said they were going to invest, while realised investment shows what they actually invested. For the last 20 years approved and realised investment has been quite closely matched. The major exception is from 1995-97. It was during this period that Turkey and the EU formed a customs union, which was associated with a wave of new announcements of manufacturing investment in Turkey. However, clearly investors' perceptions of the opportunities afforded by investing in Turkey did not meet the reality of the situation and most of the new investment was not realised. This indicates that the government was unable to facilitate the large interest shown by inward investors into real investment.

‡ Turkey was one of only 4 countries out of 24 OECD economies that on balance reduced obstacles to trade over the 1980s - the other 3 were Japan, Australia and New Zealand (Wade, 1996: 69).

Figure 1: Foreign Direct Investment in Turkey, 1980-2000, US$ million[§]



Source: GDFI (www.treasury.gov.tr).

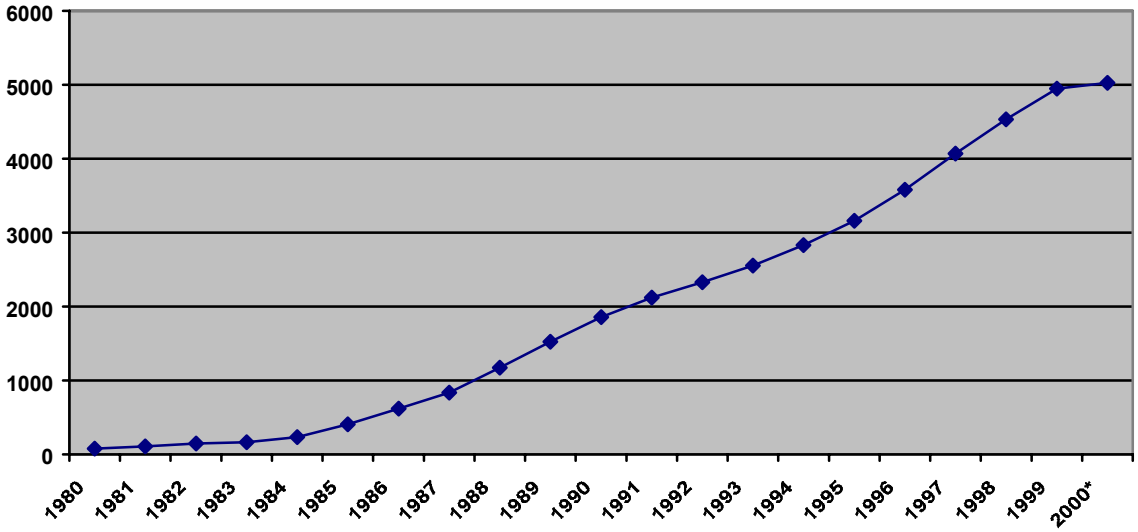
A different picture is presented, though, if we look at the number of FDI companies in Turkey over time. From Figure 2, we can see that the number of foreign equity companies[**] has increased continuously since the mid-1980s. In fact, while the number of new companies with foreign equity was around 300 per year from the mid-1980s to mid-1990s, since 1995 this Figure has increased to almost 450 per annum.

In other words, while data on FDI flows shows FDI in Turkey to be static in the 1990s, the number of companies with foreign capital is reaching record levels. In total, in early 2000 there were over 5,000 foreign equity companies in Turkey.

[§] The GDFI informs us that FDI in petroleum and refining activities are not recorded in the FDI figures. The cumulative FDI in this sector is $1.1 billion.

[**] Foreign equity companies are companies in Turkey recorded by the General Directorate of Foreign Investment (GDFI) that have foreign capital. The GDFI screens all foreign investment.

Figure 2: Cumulative number of foreign equity companies in Turkey, 1980-2000



Source: GDFI (www.treasury.gov.tr) *March 2000.

If we look at the main sources of FDI using data supplied by the General Directorate of Foreign Investment (GDFI),[††] we can see that European countries dominate FDI in Turkey (Table 1). France and Germany are the major investors in Turkey in terms of approved investment.[‡‡] In terms of the number of foreign equity companies, Germany is by far the most important source of FDI - accounting for almost 18% of all projects in Turkey.

Table 1: Main sources of FDI in Turkey, cumulative to March 2000

Country	Approved investment, US$m	Number of foreign equity investment projects
France	5,364.78	243
Germany	3,487.14	897
US	3,028.38	316
Netherlands	2,972.69	316
Switzerland	2,001.55	198
UK	1,825.21	317
Italy	1,598.26	182
Japan	1,284.24	49
Other countries	4497,98	2,506
Total	**26,060.4**	**5,024**

Source: GDFI (www.treasury.gov.tr).

†† The GDFI is in charge of co-ordinating FDI in Turkey, reviewing projects submitted for approval and actively encouraging such investment. It advises and assists investors with obtaining necessary approvals and permits, searching for locations, and identifying Turkish partners and projects. The GDFI also provides incentives.

‡‡ Because of the absence of a bilateral tax treaty until 1998 with the US, much U.S.-origin capital has been invested in Turkey through third-country subsidiaries. By unofficial estimates the U.S. is actually the largest source of foreign investment in Turkey. (US Department of State, 2000).

Table 2 shows the breakdown of FDI by sectors and sub-sectors. Manufacturing and services dominate FDI in Turkey and there has not been much change in their share of total FDI over time. The Table also shows the contribution of foreign capital in the total capital of the foreign equity ventures for each sector. This gives us an accurate indicator of the role of joint ventures in FDI in Turkey.

Table 2: Breakdown of actual FDI by sub-sector (1980-March 2000)[§§]

Sector	Number of projects with foreign equity	% of total FDI	% of FDI in total capital of projects
Agriculture & Mining	**186**	**1.3%**	**49%**
Manufacturing	**1,251**	**44.4%**	**50%**
of which:			
Food & Beverage	146	5%	50%
Tobacco	10	2.8%	91%
Textiles & garments	220	2.2%	36%
Chemicals	165	8%	79%
Plastics	52	2%	88%
Cement	9	2.8%	46%
Iron and Steel	15	1.9%	19%
Electrical machinery	69	1.9%	65%
Electronics	72	1.7%	70%
Automotive	28	8%	45%
Auto side industries	102	2.9%	53%
Services	**3,587**	**54.3%**	**63%**
of which:			
Trade	1,949	9%	77%
Hotels	279	2.6%	61%
Communication	14	1.7%	30%
Financial services	37	18.2%	75%
Investment finance	47	4.5%	30%
Social services	216	10.6%	77%
TOTAL	**5,024**	**100%**	**56%**

Source: GDFI (www.treasury.gov.tr).

In the 5,024 foreign equity ventures, foreign capital accounted for 56% of the total. Another way of looking at this is that FDI leveraged an additional 44% of domestic investment, which shows the extent of joint ventures between foreign owned and Turkish firms and the spill-over contribution of FDI to Turkey's economy. In fact, up to half of all foreign equity ventures have been joint ventures (Tatoglu and Glaister, 2000).

However, government investment agencies across the world only record joint ventures that involve foreign capital, and therefore do not capture new forms of investment that have no cross-border capital flows. To gain a more detailed picture of FDI in Turkey we monitored FDI projects in Turkey in the first half of 2000 using media searches.

§§ This Table is derived from data in Turkish Lira. The data therefore does not show the true market value of past FDI, especially given the rapid depreciation of the Lira.

Table 3 shows 21 announced FDI projects, many of which will not be recorded in official balance of payments data or by the GDFI. The projects range from expanding foreign companies' presence in the Turkish domestic market to facilitating access of Turkish firms to overseas markets.

Perhaps the most significant examples are the joint venture between DuPont and Sabanci, which expects to have $1 billion revenues from sales in Europe, Middle East and Africa (EMEA) and the announced $1.5 billion German investment in a power station. In the majority of cases the foreign companies are providing technology, market access and know-how to their Turkish partners – key examples of new forms of investment. In fact, we recorded only 3 greenfield projects.

The most important sector for projects is the information technology & telecommunications (IT&T) sector, which attracted one-third of the projects we monitored. This reflects the rapid growth of new economy activities in Turkey, in particular mobile telecommunications, e-business, Internet, and banking.[***] The next most important sectors were automotive and electronics.

While focus on FDI capital flows alone indicates that Turkey has become less successful in attracting FDI over time, our analysis of the number of foreign equity companies, joint ventures, and new forms of investment suggests that foreign companies are playing a major role in the Turkish economy.

Table 3: FDI projects in Turkey in first half 2000

Foreign investor	County	Turkish Partner	Type of FDI	Sector	Activity
EMC	US	Meteksan Sistem	Strategic partnership	Software	Data infrastructure products and services in Turkey
Louis Dreyfus Plastics Corporation	US	Ram (Koc Holding)	Strategic partnership	Trading	Expand Ram's network in Russia, CIS, Mediterranean
Balfour Beatty	UK	Garanti Koza (Koc Holding)	49% ($12.4m) acquisition	Construction	Koza will be managed on the basis of co-ownership
Miller Brewing Company	US	Efes Beverages	License agreement	Food & Drink	Produce "Miller Genuine Draft" in Turkey
France Telecom and Vivendi (planned)	France	Turk Telekom	20% ($4bn est.) acquisition	Telecommun ications	Strategic share in Turk Telekom

[***] Turkey has the fastest growing mobile phone, Internet, and IT markets in Europe. Mobile phone penetration was 15 million by mid-2000, the IT market has being growing at 25-30% per year for the last five years, 20 million people are expected to have Internet access by 2002, and one-quarter of Turkey's 2.5 million SMEs will have Internet access by 2001 (US Department of State, 2000). Turkey's young, technologically open population is driving demand and in the area of e-commerce Turkey's leading banks are amongst the most innovative in Europe.

Ritz-Carlton Hotel Company	US	Suzer Group	Strategic partnership	Tourism	To open Turkey's first five-star super deluxe hotel
First Choice Holidays	UK	Ten Tours	100% (£77m) acquisition	Holiday travel	Expand European presence
Vision Tech	Israel	Vestel	Strategic partnership	Information technology	Supply technology for Vestel's new generation TV
DuPont	US	Sabanci	Joint venture	Synthetic materials	Export to EMEA market. $1bn revenues, 4500 jobs
Polgat Company	Israel	Guney Sanayii (Baser Holding)	45% acquisition	Textiles	Access to US market and knowledge transfer
Microsoft, Compaq, Nortel Networks	US and Canada	Dogan Media Group	Strategic alliance	Internet	Set up Internet network.
Microsoft, Hitachi and Intel	US and Japan	Vestel	Strategic alliance	Electronics and IT	
Rio Tinto	Canada	Anatolia Minerals Ltd	Strategic alliance ($0.5m shares)	Mining	Rio Tinto provide $1.75m for metal exploration
Foreign investor	**County**	**Turkish Partner**	**Type of FDI**	**Sector**	**Activity**
Autoliv	Sweden	None	Expansion	Auto components	$10m investment
LG	S. Korea	None	Greenfield	Electrical	
Steag	Germa ny	None	Greenfield	Power station	$1.5bn investment planned
Daewoo Trucks	S.Korea	Sanko Otomotiv	Licensing joint venture	Automotive	New plant in south east Turkey producing trucks
Scenix	US	Arcelik	Strategic alliance	Internet / white goods	Develop and produce internet enabled household appliance
Pixelpark (Bertelsmann)	US	Turport (Medya Holding)	75% stake in joint venture	e-business	e-business strategy support for Turkish business
Toyota	Japan	Sabanci	Increase share in joint venture	Automotive	Expansion of automotive production
Alba / Pace Micro Technology	UK	Vestel	Strategic alliance	Electronics	

The role of FDI in leveraging domestic capital investment and anecdotal evidence on the contribution of new forms of investment to the technology, know-how and market access of Turkish firms suggests that FDI is making an important and growing contribution to the competitiveness of the Turkish economy. In fact, foreign affiliates account for nearly 20%

of total research and development (R&D) expenditure in Turkey and for over 70% of patent applications to the European Patent Office. This is higher than every other country in the OECD except Iceland (OECD, 1999a; 1999b)

However, the importance of foreign investment in Turkey does not necessarily mean that Turkey has performed as well as it should have in attracting FDI.

2.3. Turkey's performance relative to competitor locations

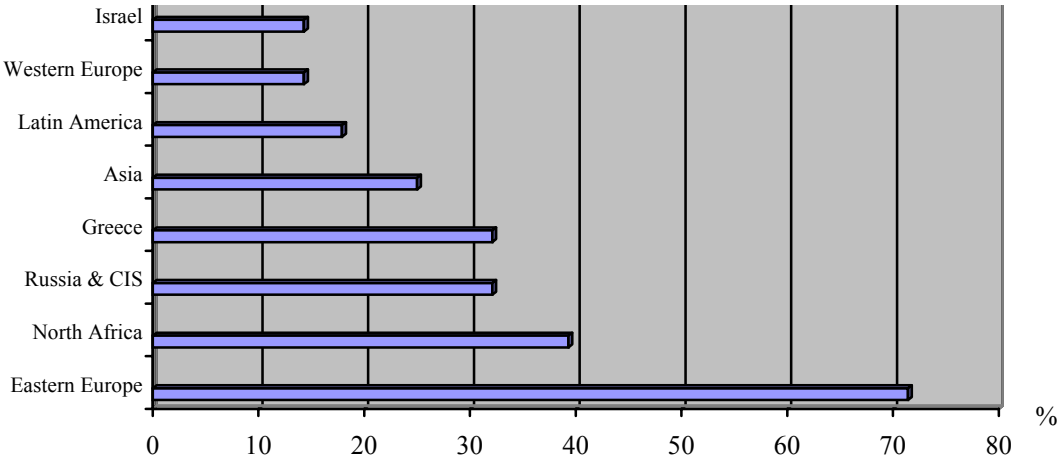
In evaluating Turkey's performance relative to other countries it is important that Turkey should be compared with competitor locations for FDI. The FDI strategies of MNCs are in most cases regionally specific (Thomsen, 2000; Ruigrok and Tulder, 1995) and often geographical proximity at the sub-regional level is a key factor in investment location. It therefore does not make sense to compare the performance of Turkey in attracting FDI with Latin American or Asian countries as for most FDI projects they are simply not competing with Turkey and the regional FDI environments are very different.

There are also major differences in national economies and FDI needs to be adjusted to take into account these differences. For example, comparing FDI in Slovenia with FDI in Russia would be meaningless unless we take into account the size of their respective economies. As Thomsen (2000: 17) argues: "What matters for host developing countries is how much investment they receive relative to the size of their economies. Market size is the primary determinant of the global distribution of FDI flows."

2.3.1. Competitor FDI locations

To understand Turkey's key competitors for FDI, in our 30 interviews with senior MNC executives we asked the question *"Which countries is Turkey competing with as a location for FDI?"* As Figure 3 shows, over 70% of respondents thought Eastern Europe was a key competitor for FDI in Turkey, followed by North Africa, Russia & CIS, and Greece. In other words, Turkey is competing against countries in the main geographical regions it borders and primarily with countries of a similar level of economic development. Hungary, Poland and the Czech Republic were cited most often as the main East European competitors to Turkey.

Figure 3: Turkey's key competitors for FDI (% of respondents citing country)



The main exception is the Middle East – only 10% of respondents saw this region as a competitor to Turkey. A key reason is the lack of economic integration and (related) poor political relations with Turkey. Israel was the most frequently cited competitor country in this region.

Asia and Latin America are not considered key competitors by 70-75% of our interview respondents, which supports previous research that MNCs are adopting regional strategies. Our interview respondents mentioned India, China, Brazil and Mexico as the main competitors in these two regions. The recently announced Mexico-EU free trade area is likely to improve the competitive position for FDI in Mexico vis-à-vis Turkey and the CEECs.

Interestingly, West European countries, excluding Greece, were seen as competitors by only 14% of respondents. This suggests that MNCs are:

- **Segmenting the European market** into West and East, most likely due to different levels of economic development (and also into North and South for activities such as call centres and shared service centres, due to geographical and cultural differences).
- **Adopting a regional division of labour** within Europe, with CEECs-Turkey competing for manufacturing activities and West European countries competing for high tech manufacturing and knowledge intensive activities. In fact, Portugal, Spain and Italy were the only West European countries specifically mentioned as competitors to Turkey – Portugal and Spain are the lowest cost locations in Western Europe and Italy is more geographically proximate to Turkey and is one of Turkey's key competitors in several industries (textiles, ceramics, and footwear).

2.3.2. Performance in attracting FDI

Table 4 compares FDI in Turkey and its key competitor locations, using balance of payments FDI data as provided by UNCTAD.

Table 4: FDI in Turkey and 9 Competitor Locations, US$ million

	1987-92 per annum	1993	1994	1995	1996	1997	1998	1999	Total 1993-9	% of total 1993-9	Total FDI/ GDP*
Poland	183	1715	1875	3659	4498	4908	6365	7500	30520	25.99%	19.25%
Russia	na	1211	640	2016	2479	6638	2761	2861	18606	15.85%	6.73%
Hungary	675	2339	1146	4453	2275	2173	2036	1944	16366	13.94%	34.23%
Czech	533	653	869	2562	1428	1300	2720	5108	14640	12.47%	25.97%
Israel	187	429	432	1337	1382	1622	1850	2256	9308	7.93%	9.26%
Greece	938	977	981	1053	1058	984	700	900	6653	5.67%	5.51%
Turkey	**578**	**636**	**608**	**885**	**722**	**805**	**940**	**783**	**5379**	**4.58%**	**2.71%**
Romania	61	94	342	420	265	1215	2031	961	5328	4.54%	13.96%
Egypt	806	493	1256	596	637	888	1077	1500	6447	5.49%	7.79%
Slovakia	91	168	245	195	251	206	631	322	2018	1.72%	9.91%
Bulgaria	34	40	105	90	109	505	537	770	2156	1.84%	17.59%
Total	4086	8755	8499	17266	15104	21244	21648	24905	117421	100.00%	10.55%

Source: Derived from UNCTAD (2000; 1999); World Bank (2000) * 1998 GDP data.

We can see that Turkey was the fourth major destination for FDI from 1987-1992, but only the 8th major location from 1993-1999. The key reason for this change in position was sustained growth of FDI in several CEECs and Israel.††† Over this period, Poland attracted nearly six times more FDI than Turkey. When adjusted for GDP Turkey is by far the worst performing country. Hungary, Czech Republic, Poland, Romania and Bulgaria were the best performing countries. As a proportion of GDP, Hungary attracted almost 13 times more FDI than Turkey from 1993-1999.

In fact, as Table 5 shows, Turkey has performed worse than every region in the world relative to the size of its economy. In terms of per capita FDI, which takes into account population size as a determinant of FDI (Bende-Nabende, 1999), Turkey has also performed worse than almost every region in the world and far worse than its key competitors. By 1996, Hungary had attracted 16 times more FDI per capita as Turkey and more surprising is the fact that Africa attracted similar levels of FDI per capita as Turkey.

Table 5: The role of FDI in the key regions of the world

	FDI inward stock/GDP (%) 1998	FDI inward stock/capita ($) 1996
World	13.7	528
Developed countries	12.1	2425
Developing countries	20	194
Africa	21.1	86
Latin America and Caribbean	19.5	660
Developing Europe	15.7	347
Asia and the Pacific	20.2	150
West Asia	7.6	259
Central Asia	25.6	71

††† The growth of FDI in Israel was primarily due to acquisitions of Israeli companies in the information technology sector and large semiconductor fabrication projects.

South, East and South-East Asia	23.3	143
Pacific	29.4	618
Central and Eastern Europe	12.1	151
Hungary	33.2	1490
Czech Republic	26.1	537
Poland	15.1	339
Turkey	**3.8**	**92**

Source: UNCTAD (1998).

2.3.3. Performance in attracting privatisation and independent FDI

To gain a more accurate picture of the comparative performance of Turkey in attracting privatisation and independent FDI, we used data from the IFC and World Bank to separate the two types of FDI. Table 6 compares FDI in Turkey with FDI in the CEECs. In terms of total privatisation-related FDI, the CEECs attracted three times more than Turkey relative to GDP. If we look at just independent FDI then Turkey has been more successful.

Table 6. Total and independent FDI in Turkey and CEECs, 1988-1995

	Total FDI	Privatisation related FDI	Independent FDI (non-privatisation)	Privatisation/ GDP	Independent FDI/ GDP
Turkey	$7.6bn	$1.2bn	$6.4bn	0.6%	3.2%
CEECs	$36bn	$16.4bn	$19.6bn	1.9%	2.3%

Source: Derived from: IFC (1997); World Bank Privatisation Database, GDFI.

However, around 60% of FDI in the CEECs has flowed into just three countries: Poland, Hungary and the Czech Republic. If we compare Turkey to Hungary - the most successful CEEC in attracting FDI – then it is clear that Turkey has greatly under-performed. Table 7 shows that relative to the size of their economies, Hungary has attracted over 20 times more FDI than Turkey and still 6.5 times more FDI when extracting privatisation related flows.

Table 7. Total and independent FDI in Turkey and Hungary, 1991-1997

	Total FDI	Privatisation related FDI	Independent FDI (non-privatisation)	FDI/GDP 1997	Independent / 1997 GDP
Turkey	$7bn	$1.2bn	$5.8bn	0.6%	2.9%
Hungary	$15bn	$6.4bn	$8.6bn	14%	18.8%

Source: Derived from GDFI, World Bank Privatisation Database, ITD.

To analyse in more detail how Turkey has performed in attracting mobile investment, we monitored manufacturing FDI projects announced in the CEECs and Turkey in the first half of 2000. We recorded 27 projects, which while capturing only a small proportion of total projects, provides an indication of market trends and includes many of the more important projects.

Table 8 reinforces our previous analysis that Hungary, Czech Republic and Poland are the major locations for mobile FDI projects. We can describe these three countries as first-tier investment locations in the region. Slovakia, Turkey and Estonia represent second-tier locations. It appears that these 6 countries account for almost all FDI projects in the CEEC-Turkey region.

Table 8: Mobile investment projects announced in first half 2000*

Company	Origin	Sector	Location	Capital	Jobs	Short listed countries
Nemak	US/ Mexico	Auto parts	Czech R.	$30m	200	Czech R., Hung., Pol., Slov.
ARN	Norway	Alum. Recycling	Czech R.	$12m	50	
Foster Wheeler	Italy	Polypropylene	Czech R.			
Philips	Holland	Elec. Components	Czech Rep.	$600m	1,000	
Mitsubishi Elec.	Japan	Auto electronics	Czech Rep.	$33m	280	
Lanna Svets	Sweden	Metal manufact.	Estonia			
INCAP	Finland	Electronics	Estonia			
Plywood	Finland	Wood manufact.	Estonia			
Westcast/Linamar	Canada	Auto parts	Hungary		550	Hungary, Poland, Czech R.
Motorola / DBTd	US/Taiwan	Mobile phone	Hungary	$80m		CEECs (not Turkey)
Taiho Kogyo	Japan	Auto parts	Hungary			
Jabil Circuits	US	Man. Services	Hungary	$80m	1000	
Artesyn Tech.s	US	Telecom man.	Hungary	$20m	1,200	
Nokia	Finland	Telcoms	Hungary		500	
Esmar	Spain	Elec. Components	Hungary		250	Poland, Czech Rep.
Visteon	US	Auto components	Hungary	$62m	150	All Europe
Audi	Germany	Diesel engines	Hungary	$330m	2000	
Visteon	US	Auto components	Hungary	$18m		
Tata	India	Software	Hungary	$100m	80	
Delphi Calsonic	US/Japan	Auto components	Hungary	$80m		
Samsung	S. Korea	Elec. Components	Hungary	$21m	500	Hungary, Poland
Timken	US	Machine tools	Pol. & Rom.			Eastern Europe
Toyota	Japan	Auto assembly	Poland			
Macalux	Spain	Auto parts	Poland	$15m	30	Pol., Hung., Ger., Czech R.
Fextronics	Sweden	Industrial Park	Poland	$25m	3	Eastern Europe and CIS
Sapa	Sweden	Aluminium man.	Poland			
TRW	US	Auto components	Poland		350	Czech., Slovenia, Slov.,Pol.
Intel	US	Software	Russia		500	
VW / Porsche	Germany	Auto assembly	Slovakia			Slovakia, Portugal, Poland
Bekaert	Belgium	Auto related	Slovakia	$14		Slov., Hung., Pol., Czech R.
VW	Germany	Auto components	Slovakia	$18m	400	Poland, Hungary
Osram (Siemens)	Germany	Lighting man.	Slovakia	$2.3m		

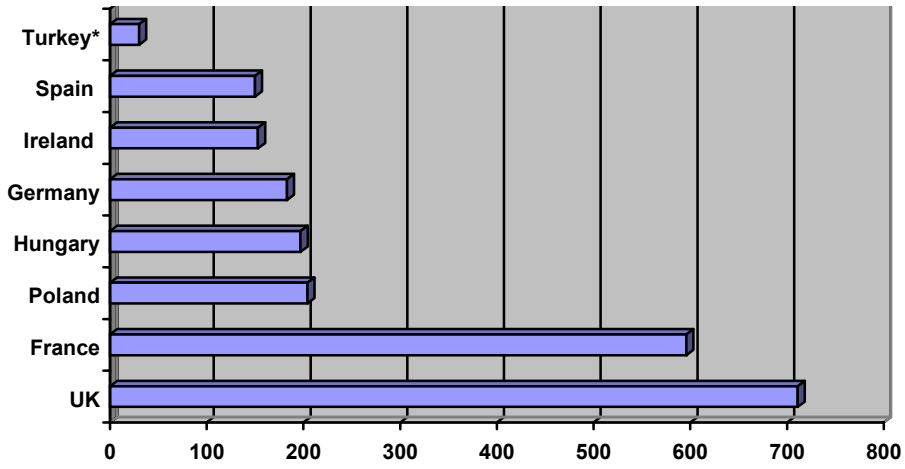
Autoliv	Sweden	Auto components	Turkey	$10m		
LG	S. Korea	Electrical	Turkey			
Steag	Germany	Power station	Turkey	$1.5bn		

Source: news media. *capital, jobs and short listed countries are estimates.

Hungary is the most favoured location, accounting for almost half of the total projects we recorded, followed by Poland. This is supported by comprehensive research by Ernst & Young, which shows that Hungary and Poland were among the top locations for manufacturing FDI projects in Europe from 1997-1999 (Figure 4).

If Turkey is to increase its share of FDI projects, it is important to understand Turkey's competitive position relative to first tier locations in the CEEC-Turkey region. At present, Turkey is losing projects to Hungary and other countries. For example, Samsung's $21 million, 500 job plant in Hungary (Table 8) is actually going to supply the Turkish market. In many cases Turkey is simply not on the investment map. In the projects where we were able to gain information on short-listed locations, Turkey was not once short-listed. This finding is reinforced by our interview results, with 85% of respondents stating that Turkey made the short list "not at all" or "to a minor extent."##

Figure 4: Manufacturing FDI projects (new and expansions) in Europe, January 1997-June 1999



* Our estimates
Source: Ernst & Young EIM cited in Corporate Location (2000).

2.4. Conclusion

Foreign direct investment plays a major role in the Turkish economy. In fact, Turkey is more dependent on foreign investors that most other countries for technological and innovation activities. However, when compared to its main competitors for inward

When companies make investment location decisions they often first make a "long list" of potential locations based on whether the location meets broad requirements. They then reduce this list to a "short list" of locations that meet the more specific requirements of the internationalisation strategy and the particular project (Loewendahl, 2001).

investment, which we identified to be primarily in Eastern Europe, Turkey has been less successful in attracting FDI relative to the size of its economy and population. A key reason is the minimal level of privatisation-related investment in Turkey.

When we compared Turkey with its main competitor countries for FDI in the CEECs, Turkey's performed far worse even when compensating for privatisation FDI. Even taking into account the possible leverage on independent FDI of privatisation-related flows (Sader, 1995), the present privatisation process in Turkey is unlikely to improve Turkey's long term performance in attracting FDI relative to its key competitors.

It is therefore essential to understand the key factors influencing the location of FDI and to explain why Turkey has failed to attract the levels of FDI of its major competitors.

3. Explaining Turkey's performance

3.1. Introduction

Turkey represents a paradox. According to Institutional Investor Americas (1999):

> Turkey has many advantages to offer foreign investors: a domestic market of 64 million people, proximity to the huge markets of Europe, the Commonwealth of Independent States, the Middle East and North Africa, low labour costs, a well-educated managerial class, state-of-the art telecommunications networks, and modern infrastructure. Foreign investors can freely move capital goods, capital, profits, and dividends in and out of the country, and have the same rights, exemptions, and privileges as Turkish investors."

Yet at the same time we found that Turkey has under-performed in attracting FDI. This chapter aims to understand this paradox through first identifying the key location factors influencing MNCs' decision to invest in one country in preference to another, and second use this analysis to evaluate Turkey's competitive location position. We aim to highlight the key obstacles to FDI in Turkey.

3.2. Key location factors in investment location decision making

The emphasis of most literature in international business studies is on theories explaining why firms engage in FDI rather than where they locate. The literature, as represented by Dunning's (1977; 1988) OLI paradigm, does not explicitly consider *how* the firm decides *where* to locate its investment. To explain investment location we need to understand the motivation driving firms to invest overseas and why one location is selected in preference to another.

According to PricewaterhouseCoopers (1999b): "The company needs to find business environments that reliably match a complex array of success factors unique to the competitive strategy and specific project of the enterprise." However, traditional international business theories have tended to neglect considerations of corporate strategy in investment location decisions (European Commission, 1998; Mucchielli, 1991). This is a major short-coming as a country's attractiveness for inward investment cannot be defined

without reference to company investment strategies (Michalet, 1997: 23), with investment location often dependent on the overall strategy of the firm (see Loewendahl, 1999 for the case of Siemens).

Dunning (1998) has identified four generic types of strategic motives for international investment: market, efficiency, resource, and asset seeking FDI. In terms of market (horizontal) and efficiency (vertical) seeking investment, FDI reflects a trade-off between proximity to market and economies of scale from concentrating production (Di Mauro, 1999; Markusen and Venables, 1996; Brainard, 1993).

The importance of market seeking FDI has been indicated in many empirical studies. FDI flows have been shown to correlate with market size (Di Mauro, 1999; Bende-Nabende, 1999; UNCTAD, 1998; Mody and Wheeler, 1992) and firm-level surveys have also emphasised the over-riding importance of market seeking motives (e.g. Michalet, 1997; Commerzbank, 1997 cited in OECD, 1997; NEI, 1992; IBB, 1991). Market seeking FDI provides an explanation for the two-way investment between developed countries (see Brenton, 1996 for a theoretical overview).

Efficiency seeking FDI stresses differences in factor costs, but many studies have shown that FDI in developing countries is primarily market seeking (e.g. Estrin et al, 1997; Agarwal, 1997; Yeung, 1996). Cost differences are only likely to play a critical role in determining investment location when the investor needs to choose between short-listed countries, which are likely to be part of the same, sub-regional market (Loewendahl, 2001).

Asset seeking FDI is the most recent motive for FDI to be identified. It refers to a strategy that aims to access and exploit technological assets in overseas countries. Asset seeking FDI is largely in the form of M&As and technology agreements, but there has also been in recent years a rapid growth in overseas R&D investments. Developed countries are the main recipients for R&D investment, but countries such as Hungary, India and Brazil are also attracting more and more R&D projects.[§§§]

[§§§] See Loewendahl (2001) for a detailed analysis of asset seeking FDI.

Table 9: Strategic and project determinants of country attractiveness for FDI

FDI determinants	Corporate strategy	Key location factors in host country
Economic determinants - Economic liberalism (tariff and non-tariff barriers; privatisation, foreign exchange policy; taxation) - Performance (GDP growth, inflation, government, internal and external debt) - Long term strategy (adjustment and stabilisation; local market, exports) - FDI track record - Factors in right side of Table - Telecommunications infrastructure **FDI enabling environment** - Investment promotion - Investment facilitation - Investment incentives - Corruption and administrative costs - Property and site provision - Social amenities - After-care services **Political and institutional** - Political system - Government attitude to foreign investment - Tensions among socio-economic groups - Law and Order: the judicial system and dispute settlement - Rules of entry and operation - Policies on functioning and structure of markets (especially competition policy, mergers & acquisitions, labour markets) - International agreement on FDI - Coherence of FDI and trade policies - Cultural factors and quality of life	**Market seeking** **Efficiency seeking** **Resource seeking** **Asset seeking** economies	- Market size - Market growth - Access to regional or global markets - Country-specific consumer preferences - Structure of markets - Strength of indigenous business - Costs of resources and assets, adjusted for labour productivity - Other input costs, such as transport, and intermediate products - Membership of a regional integration area for economies of scale - Raw materials - Low cost, unskilled labour - Skilled labour availability - Quality universities and research institutes - Large supply of graduate labour - Created assets including innovative capacity, technological adoption, marketing networks, technical skills, work and cultural attitudes, agglomeration - clusters and critical mass in R&D and FDI

Source: Developed from PricewaterhouseCoopers (1999b); Moran (1999); Dunning (1998); UNCTAD (1998); Michalet's (1997); Christodoulou (1996).

These generic strategies cannot be taken in isolation from one another. There is a constant trade-off in MNC location decision-making between proximity and concentration (Di Mauro, 1999: 5), revenues and costs (Haigh et al cited in Thomsen and Woolcock, 1993: 38), and exports and selling locally (OECD, 1998a: 20). As argued by Michalet (1997: 11),

multinationals "more and more seek sites that offer *both* market access and conditions for world-competitive production…Multinationals are using both strategies at the same time."

In fact, we would argue that MNCs are increasingly making investment location decisions based on a regional or global strategy that integrates market, efficiency, *and* asset seeking motives. The ideal location should offer access to markets, an efficient production base, and at the same time the technological assets that can contribute to the company's network of critical capabilities across the world.

Building on existing literature, Table 12 highlights the main generic determinants of FDI, which we divide into economic, the enabling environment, and political institutional factors, and key location factors specific to the particular internationalisation strategy of the firm. We will use Table 9 as a template for evaluating Turkey's competitive location position in the next section.

3.3. Turkey's competitive position

In this section we evaluate Turkey's competitive position in meeting the requirements of MNC strategy. We examine the attractiveness of Turkey for market, efficiency and asset seeking FDI before assessing Turkey relative to competitor locations in meeting the enabling environment and political-institutional determinants of FDI.

3.3.1 Attractiveness to multinational corporations

In our interviews with the senior executives we asked the question *"As a location for market, efficiency, and asset seeking FDI in what order would you rank Turkey and its main competitors for investment?"* We gained 19 complete responses that ranked Turkey against three CEECs and Egypt. Table 10 shows the results.

We can see that Turkey is considered the most favourable location for market seeking FDI by 53% of respondents, compared to 32% for the CEECs. In terms of efficiency seeking FDI, 40% of respondents ranked Turkey first place compared to 60% of respondents ranking the CEECs first place. Turkey and the CEECs were ranked equally as a location for asset-seeking investment. Egypt was ranked as the least attractive location in every case.

Table 10: Rank of Turkey and key competitors as a location for market, efficiency and asset seeking FDI (% of total respondents)

Country*	Rank first			Rank second			Rank third		
	Market seeking	Efficiency Seeking	Asset seeking	Market Seeking	Efficiency seeking	Asset seeking	Market seeking	Efficiency seeking	Asset seeking
Turkey	53%	40%	50%	32%	47%	50%	16%	13%	0%
CEECs (3)	32%	60%	50%	47%	33%	50%	21%	7%	0%
Egypt	15%	0%	0%	21%	20%	0%	63%	80%	50%

* CEECs (3) are Czech Republic, Hungary and Poland.

Our findings support an earlier study of 90 MNCs, which found Turkey to be the most attractive location in the CEECs-Turkey-North Africa region for American firms and the

second most attractive location for European firms for market seeking FDI (Table 11). Turkey is ranked slightly less attractive as a location for efficiency seeking FDI

Table 11: Attractiveness of countries as seen by European and US firms

European firms		American firms	
Market seeking	Efficiency seeking	Market seeking	Efficiency seeking
Portugal	Poland	**Turkey**	Hungary
Poland	**Turkey**	Hungary	Poland
Turkey	Portugal	Poland	**Turkey**
Hungary	Hungary	Russia	Portugal
Russia	Russia	Portugal	Russia
Slovakia	Slovakia	Egypt	Egpyt
Egypt	Lithuania	Ukraine	Ukraine
Morocco	Ukraine	Morocco	Tunisia
Ukraine	Egypt	Tunisia	Morocco
Tunisia	Morocco	Slovakia	Lithuania
Lithuania	Tunisia	Lithuania	Slovakia

Source: Michalet (1997).

Overall, based on the perceptions of MNCs we would expect Turkey to have attracted similar levels of FDI to the leading locations in Central and Eastern Europe.

3.3.2. Key location advantages for market seeking FDI

To assess Turkey's location advantages for market seeking investment we compared Turkey's market size and performance with 11 other countries, including Turkey's main regional competitors for FDI and Latin American and East Asian emerging countries. Table 12 shows that Turkey is among the largest emerging markets in the world.[****]

Table 12: The Market size of Turkey and 11 other countries in 1998

Country	Size of GNP (billions) 1998		GNP per capita (1998)		Population size (millions) 1998
	US$	US$ PPP	US$	US$ PPP	
Brazil	758.0	1,021.4	4,570	6,160	166
Mexico	380.9	785.8	3,970	8,190	96
South Korea	369.9	569.3	7,970	12,270	46
Turkey*	**200.5**	**404**	**3,160**	**6,470**	**63**
Poland	150.8	260.7	3,900	6,740	39
Thailand	134.4	357.1	2,200	5,840	61
South Africa	119.0	288.7	2,880	6,990	41
Iran	109.6	-	1,770	5,690[1]	62
Malaysia	79.8	155.1	3,600	6,990	22
Egypt	79.2	192.5	1,290	3,130	61
Czech Rep.	51.8	108[1]	5,040	10,380[1]	10
Hungary	45.6	73[1]	4,510	6,970[1]	10

[****] Turkey's GNP and per capita income are underestimated. According to the US Department of State (2000), the private sector contributes to an "unregistered" economy, which increases GNP by up to 50%. A recent study has attempted to calculate a more accurate picture of incomes in Turkey taking into account the informal economy. The study concluded that of the 63 million people living in Turkey, income per capita of 15 million people is $15,000 (Le Figaro, 2000).

Source: World Bank (2000; 1999), *PPP data is GDP 1997, ¹1997.

Table 13 shows an impressive economic performance in Turkey over time and that it is perhaps the most successful example of export-led industrialisation outside of East Asia.

Table 13: Trends in economic performance of Turkey and 11 other emerging markets

Country	Average annual GDP growth		Average annual manufacturing growth		Average annual growth in exports	
	1980-1990	1990-1998	1980-1990	1990-1998	1980-1990	1990-97
South Korea	9.4	6.1	13.0	6.9	14.9	12.3
Thailand	7.6	5.7	9.5	7.7	14.1	14.9
Turkey	**5.4**	**4.2**	**7.9**	**5.9**	**14.2**	**11.2**
Egypt	5.4	4.2	-	5.3	-3.7	4.3
Malaysia	5.3	7.4	8.9	10.1	8.6	16.8
Brazil	2.7	3.2	1.6	2.5	5.1	8.2
Poland	2.2	4.6	-1.5	3.5	1.4	11
Czech Rep.	1.7	0.9	-	-	-	-
Iran	1.7	3.6	4.5	4.9	1.1	1.6
Hungary	1.3	0.5	-	6.5	1.2	6.2
Mexico	1.1	2.5	1.5	3.6	6.3	20.5
South Africa	1.0	1.9	1.1	1.1	0.7	4.4

Source: World Bank (2000).

The prospects for "tremendous growth" in Turkey's economy led to its designation by the U.S. Department of Commerce as one of the world's ten "Big Emerging Markets" (US Department of State, 2000). The UK Government's Export Forum has singled out Turkey as being one of the 12 international markets that offered significant trade and investment opportunities for British firms (DTI, 1999). In fact, the Turkish government forecasts Turkey's per capita income to reach $20,000 by 2020, making Turkey the 10th biggest economy in the world.†††† While this is based on a scenario of 6-7% growth per annum, it appears to be shared not only by the US and British governments but also by major private sector organisations. ING Barings (1999), for example, has forecast Turkey to converge to the average of 3 lowest income countries in the EU in about 25 years – before most of the other 12 candidates to join the EU.

In terms of market seeking investment, we can conclude that Turkey has the strongest competitive position as a location for FDI in its region due to the combination of large and dynamic economy and large population with mid-level per capita incomes.‡‡‡ Turkey can in fact be considered a converging rather than an emerging market.

†††† The South Eastern Anatolia Project (GAP) will increase regional per capita income in the South East of Turkey by almost 3 times and generate job opportunities for 3.3 million people. The estimated cost of GAP is $32 billion, of which 43% of total investment has been realised so far (Kiminvest, 2000).

‡‡‡ Empirical studies examining foreign firms investing in Turkey have found market-seeking factors to be the dominant motivation. Erdilek (1982) and Demirbag et al. (1995) from surveys of 93 foreign firms in Turkey found meeting domestic demand were the key reasons for investing. Tatoglu and Glaister (2000), in a more recent survey of 98 foreign firms, found the most important strategic motives for FDI in Turkey were to gain access to new markets and to enable faster market

3.3.3. Key location advantages for efficiency seeking FDI

Key location factors for efficiency seeking investment include labour costs, skills and availability, and access to international markets (Table 9). In terms of labour costs and productivity, Table 14 shows that Turkey has higher costs than the CEECs but much higher labour productivity.

The Turkish workforce has gained a reputation as being productive, flexible, and hard working.§§§§ According to PricewaterhouseCoopers (1999a: 26): "Turkey offers a dynamic and challenging business environment in a rapidly changing marketplace…The Workforce is highly motivated, disciplined and trainable."

Table 14: Labour costs and productivity in manufacturing, 1990-94, US$ per year*

Country	Labour cost per worker in manufacturing	Value added per worker in manufacturing
Turkey	**7,958**	**32,961**
Hungary	2,777	6,106 (11,226)
Czech Republic	1,876	5,094 (8,225)
Poland	1,714	7,637 (9,034)
Greece	15,899	30,429
Ireland	25,414	86,036
Romania	1,190	3,482 (3,808)

Source: Derived from World Bank (2000); Eurostat (1999); UNIDO (1999) *data in brackets is for 1997.

Using survey data from the IMD, Table 15 compares in more detail the qualitative attributes of the Turkish labour force that are often key location factors for efficiency seeking FDI and for many types of investment project. We ranked Turkey with Czech Republic, Hungary and Poland (its three major competitors for inward investment), Ireland (which has been highly successful in attracting inward investment), and Russia (which has been unsuccessful – see Bergsman et al, 2000). We also compare Turkey with Greece (a geographically proximate location).

Table 15: Benchmarking the quality of Labour in Turkey (rank out of 47 countries)*

	Turkey	Hungary	Ireland	Greece	Poland	Czech Rep.	Russia
Labour regulations are flexible enough	**11**	5	15	32	17	19	23
Competent senior managers are available in your country	**8**	31	11	33	40	46	47
Management has significant international experience	**12**	30	7	28	40	46	37

access. They found market size and the growth rate of the economy to be key location factors influencing investment in Turkey.

§§§§ The latest data from the International Labour Organisation shows that Turkish people are the second most hardworking in the world. Nearly 90% of Turkish men and 80% of Turkish women work for more than 40 hours a week.

Qualified engineers are available in your country	**13**	1	21	16	26	33	43
Qualified IT employees are available in your country	**12**	2	21	25	16	31	36
Total	**56**	69	75	134	139	175	186
Average score	**11.2**	13.8	15	26.8	27.8	35	37.2

Source: Derived from IMD, 2000. * The IMD surveyed 3,263 senior managers in 47 countries. Rank 1 is best in the world. Rank 47 is worst.

The results are perhaps surprising, with Turkey ranking above all the countries. Only Hungary and Ireland are close to matching Turkey's labour quality. Turkey is among the top 13 locations in the world on every criterion. This was supported in our interviews, with 45% of respondents stating that the skilled and educated workforce was a key strength of Turkey as an investment location (see SWOT analysis in the Appendix).

Efficiency seeking, export-oriented investment strategies depend on access to an integrated regional market. According to the OECD (1998a: 26), regional integration can lead to horizontal reorganisation (each country producing a different version of a product) and vertical reorganisation (each country responsible for one stage of production). In both cases, FDI should be encouraged (see Bende-Nabende, 1999; Di Mauro, 1999; Brenton, 1999; EC, 1998: 142).

In 1996 a customs union between Turkey and the EU came into effect, which led to protection for EU countries falling from 5.9% to zero for most products and 3rd country protection for industrial products falling from 10.8% to 6%. For firms with a market-seeking strategy, the customs union should in theory encourage local production by 3rd countries (like the US and Japan) due to the increased competitiveness of EU products.

For firms with an efficiency-seeking strategy inside the European market, Turkey is the only non-EU member to have a customs union with the EU. With manufacturing labour costs in Turkey half the level of Greece and Portugal and one-quarter the level of Germany, in theory the customs union should encourage FDI with Turkey becoming a production base for exporting to the rest of the EU. As Tatoglu and Glaister (2000: 4) argue: "It is expected that the customs union with the EU will spur the flow of European FDI to Turkey."

According to Michalet's (1997: 14): "The ideal core country is one that offers at the same time a large enough domestic market to justify an industrial investment, *and* a launching pad into a regional market." Our analysis of Turkey's competitive position suggests Turkey perfectly meets the requirements for an ideal core country.

3.3.4. Key location advantages for asset seeking FDI

Essential to asset-seeking investment is the engineering and science supply-side factors of the economy, and increasingly the telecommunications and Internet infrastructure. Table 16 compares key location factors in Turkey and 7 other countries. While Turkey has among the highest proportion of science and engineering students, patent applications and R&D expenditures are lower than many competitor locations. Turkey is clearly a long way behind Ireland in terms of its location advantages for asset-seeking FDI and is just about in the

same group as Czech Republic, Hungary and Poland, but is in danger of falling behind if the technology infrastructure is not improved. Table 16 also gives clear evidence why our interview respondents ranked Egypt last place as a location for asset-seeking FDI.[*****]

Table 16: Engineering and science indicators, 1987-97

Country	Science and engineering students, % of total tertiary students	Patent applications filed by non-residents	R&D expenditure, % of GNP
Russia	50	32,943	0.88
Turkey	**45**	**27,985**	**0.45**
Hungary	32	29,331	0.68
Ireland	31	82,484	1.61
Czech Republic	28	29,976	1.20
Poland	28	30,137	0.77
Greece	26	82,390	0.47
Egypt	12	706	0.22

Source: World Bank (2000).

3.3.5. FDI enabling environment

A favourable FDI "enabling environment" is a pre-condition for attracting inward investment (UNCAD, 1999). The FDI enabling environment involves the facilitation and support a location gives to inwardly investing companies. It has several components including FDI legislation and procedures, attitudes towards foreign investment, incentives, and investment promotion.

According to the US Department of Commerce: "Bureaucratic procedures related to the establishment of a foreign investment are, in general, streamlined and transparent. Turkey's foreign investment regime is among the most liberal in OECD countries" (US Department of State, 2000). An indicator of the height of administrative barriers to FDI is the ratio of implemented to approved investments. Investor-friendly countries target realisation rates of 60%-70%, and Singapore claims 80%. At the lower end of the range, it can be 15%-30% (IFC, 1997: 40). Turkey's realisation ratio is nearly 50% (derived from Figure 1), which is about average.

Turkey's incentives regime is also one of the most attractive on paper in the world.[††††] In 1995, the government announced an incentives package designed to attract investors to 20

[*****] Turkey's telecommunications infrastructure is closer to West European levels, with digitalisation higher than some EU members (Loewendahl, 1998) and off-peak Internet costs the lowest in the OECD (Economist, 2000)

[††††] In fact, we would agree with Balasubramanyam (1996: 126) who argues that Turkey's incentives and free zone may be much too generous. Kaminski and Riboud (1999: 32) find that companies in free zones do not have any incentive to develop linkages with rest of economy and may be more footloose. UNCTAD (1998: 145) supports this argument, finding that "FDI in tax havens or FDI made in response to incentives is particularly vulnerable to divestment" and the OECD (1998a: 56) states that up to 95% of inputs of foreign firms in free zones in South East Asia are imported. It is unclear what the impact of free zones is on long term competitiveness (UNCTAD, 1999: 237; Hines, 1996), and Hungary and Poland are both reducing incentives and curtailing free zones.

industrial belts across the country. The package includes grants of up to 70% of total fixed investment, customs duties and fund exemptions, VAT refunds and subsidised credits up to 40% (www.treasury.gov.tr/english/ybsweb/incentives.html). Turkey also has 17 free zones offering very generous incentives (see www.treasury.gov.tr/english/ybsweb/freezones.html).

Although Turkey has one of the world's most liberal foreign investment laws and attractive incentive regimes, the enabling environment for privatisation and infrastructure-related foreign investors has been very weak. A key obstacle has been the lack of international arbitration, which deterred such investment, especially in big public projects (Euromoney, 2000; Middle East Economic Digest, 1999; Institutional Investor Americas, 1999). This is supported by our interview results with over 50% of respondents citing legislation, regulation and bureaucracy and nearly 30% citing the slow pace of reform and political resistance as the major factors explaining Turkey's under-performance in attracting country-specific infrastructure and privatisation-related FDI.

To evaluate Turkey overall enabling environment in comparison with other investment locations, Table 19 draws on survey evidence from the IMD. On almost every criteria Turkey ranks above average out of 47 developed and emerging economies. Turkey's FDI enabling environment is only narrowly behind that of Greece and Hungary and is perceived to be far more favourable than the Czech Republic, Poland and Russia. In fact, Russia and Poland are among the worst performing countries out of the 47 in the IMD sample.

Table 19: FDI enabling environment (ranking out of 47 countries)

	Ireland	*Hungary*	Greece	**Turkey**	Czech Rep.	Poland	Russia
Protectionism does not prevent import of foreign products	5	24	14	**14**	18	38	46
Foreign investors are free to acquire control in a domestic company	2	14	15	**17**	20	38	46
Foreign companies are treated equally to domestic	6	34	15	**14**	36	45	47
Public sector contracts are open to foreign bidders	2	18	22	**15**	27	34	47
Cross border ventures can be negotiated with foreign partners without government	3	12	15	**24**	27	43	45
Investment protection schemes are available for foreign partner countries	14	1	12	**18**	24	34	47
Investment incentives are attractive to foreign investors	1	5	29	**19**	36	15	47
National culture is open to foreign influence	9	20	19	**28**	42	29	30
Immigration laws do not prevent employment of foreign labour	28	11	12	**15**	22	41	44
Total	70	139	153	**164**	252	317	399
Score	7.8	15.4	17.0	**18.2**	28.0	35.2	44.3

Source: Derived from IMD, 2000.

Another dimension of facilitating FDI is investment promotion. In our interviews, 85% of respondents when asked whether Turkey's has effective promotion replied "not at all" or "to a minor degree." Half of respondents said that the GDFI needs to be able to provide very specific, investor-related information. Similarly, almost 60% of respondents stated that there was not adequate information on Turkey. Of these, 70% said they would like more general information and 20% said they would like information on regional differences.### It is therefore not surprising over 60% of respondents when asked if Turkey has an effective image replied "not at all" or "to a minor degree."

3.3.6. Political-institutional environment

According to Michalet (1997): "an indispensable precondition for encouraging foreign investment is to have a stable political and economic climate, and a transparent and non-discretionary legal and regulatory framework." We found strong support for this argument in case of Turkey. In our interviews, political instability was cited by over 70% of respondents and economic instability by 50% as key factors reducing the level of independent FDI in Turkey. Legislation and bureaucracy was also a thought to be a key factor reducing FDI in Turkey according to almost 35% of respondents. This is despite the liberal FDI regime and broadly effective facilitation by the GDFI. Key factors identified in our interviews included political interference in FDI facilitation, weak justice system, corruption, and the inadequate enforcement of competition law and intellectual property rights. Several respondents also noted that investors' generally think the Turkish government does not view FDI favourable and mistrusts foreign companies and foreigners in general.

Our interview evidence is supported by the IMD, which found Turkey to have a very poor institutional environment when measured across 8 dimensions. Table 19 shows that Turkey ranks behind Hungary and Poland, but is still ranked slightly above the Czech Republic and Russia. The contrast with Ireland is clear.

Turkey performs particularly badly in terms of political instability and exchange rate stability. Turkey's political instability can be seen by the fact that Turkey has had 11 governments in the past 10 years. However, Poland, has had 9 government in the last 9 years but has still been successful in attracting FDI. Political instability is not a constraint to attracting FDI unless it prevents structural reform and reduces markedly policy certainty.

In Turkey, political instability has had a major impact on macro-economic instability, with the lack of structural economic reform leading to chronic inflation and exchange rate instability (Loewendahl, 1998). In Poland, political instability has not proved to be an obstacle to structural reform, with the reduction in inflation from 35.3% in 1993 to 14.9% in 1997 and simultaneous reduction in debt coinciding with a rapid growth in FDI and other capital inflows (see Orlowski and Szczepanska-Maciejuk, 1998)

According to one respondent: "We [Turkey] need to create new promotional agencies at the regional and national levels. They should focus on specific sectors and companies that may have interest in Turkey through aggressive marketing and promotion. Regions should market themselves separately, while the national government promotes Turkey in general".

Table 19: Institutional environment (ranking out of 47 countries)

	Ireland	Hungary	Greece	Poland	**Turkey**	Czech Rep.	Russia
Exchange rate stability	21	39	34	40	**43**	17	-
The public service is immune from political interference	7	29	41	24	**35**	38	27
Bureaucracy does not hinder business development	5	20	41	26	**27**	34	47
Customs administration does not hinder transit of goods	6	30	25	35	**32**	33	43
Bribing and corruption does not exist in public	17	28	36	30	**33**	41	40
Competition laws do not prevent unfair competition	9	24	37	44	**36**	40	47
Justice is fairly administered in society	10	23	26	37	**34**	41	45
Risk of political instability is very low	7	19	20	41	**43**	42	47
Total	82	212	260	277	**283**	286	296
Score	10.25	26.5	32.5	34.625	**35.375**	35.75	37

Source: Derived from IMD (2000).

Turkey's chronic inflation is a key factor explaining why Turkey has under-performed. According to Institutional Investor Americas (1999), "high inflation and past political instability has kept foreign investors away" and the IMD (2000: 24) argues that "Turkey's competitiveness is held back by the unusually high inflation rate of 65%, which prevents the country to fully exploit its formidable potential."

3.4. Conclusion

In this chapter we argued that investment location is determined by firm strategy and identified the key location factors for different strategies, which we used to evaluate Turkey's competitive position relative to other countries.

We found powerful evidence from our empirical data and interviews that in meeting the economic determinants for market and efficiency seeking FDI, Turkey's competitive position is very strong. Turkey combines a large, dynamic market with a high quality, high productivity labour force and access to regional markets. In addition, we found Turkey's FDI enabling environment to be largely favourable for independent investment when compared to competitor locations, although Turkey's investment promotion is totally inadequate. Overall, when we combine Turkey's economic location advantages with liberal FDI regulations and attractive incentives, we would expect high levels of FDI in Turkey.

However, we found that Turkey's FDI enabling environment was far weaker for privatisation-related and infrastructure investment and our competitive assessment of political-institutional factors identified many obstacles to FDI in Turkey. Table 20 summarises Turkey's competitive position in meeting the location requirements for FDI.

Table 20: Turkey's location advantages for FDI

Key location factors	Competitive position
Market seeking FDI	
Economic size	Strong
Economic growth	Strong
Population size	Strong
Per capita incomes	Medium
Efficiency seeking FDI	
Labour costs	
Labour productivity	Strong
Regional integration zone	Strong
Labour skills and supply	Strong
Asset seeking FDI	Strong
Supply of engineers and technicians	
R&D and innovation base	
Telecoms & Internet infrastructure	Strong
FDI enabling environment	Weak
FDI legislation (independent FDI)	Medium
FDI legislation (privatisation/infrastructure FDI)	
Facilitation process	
Political commitment	Strong
Incentives	Weak
Investment promotion	Medium
Institutional-Political environment	Weak
Economic instability (inflation, exchange rates, debt)	Strong
Policy certainty	Weak
Political interference, bureaucracy, and corruption	
Justice system and intellectual property rights	
Internal social tensions	Weak
	Weak
	Weak
	Weak
	Weak

Table 20 shows that Turkey's key competitive weaknesses are associated with institutional-political factors. Turkey performs worse than most of its competitors in terms of political and economic stability and we identified inflation as a particularly significant obstacle for inward investment. Other obstacles include lack of transparency, political interference, and corruption, as well as internal social tensions (see SWOT analysis in the Appendix).

Political instability and the associated uncertain investment climate have prevented Turkey from exploiting the potential of the customs union. The evidence strongly suggests that FDI in Turkey has been primarily market seeking not efficiency seeking and the Turkey-EU customs union has not led to a rapid growth in efficiency-seeking FDI.[§§§§§] As Bende-

[§§§§§] Only in the last year have major companies began to adopt efficiency seeking strategies for their Turkish operations, especially in the automotive industry. Renault awarded its first ever world product mandate outside of France to its Turkish joint venture operation, and Ford and Fiat are

Nabende (1999: Ch.7) argues, the liberalisation of trade associated with regional integration is unlikely to lead to increased FDI unless the political situation is stable and the investment climate certain.

While we found Poland and the Czech Republic to also have an unfavourable political-institutional environment, they have not suffered from the chronic inflation of Turkey, the domestic and international security and human rights concerns, and they have had greater stability in economic policy. Privatisation is a key example, with our research in this chapter stressing the policy instability and slow pace of reform in Turkey, as well as lack of international arbitration.

The uncertainty over investing in Turkey, and lack of information on what Turkey has to offer has been compounded by an almost total lack of effective investment promotion. Given these obstacles to attracting FDI, Turkey has not been able to compete successfully with the CEECs for FDI, despite its very strong underlying competitive position.

4. The IMF Agreement and EU Enlargement

4.1. Introduction

In this chapter we evaluate how Turkey's recent stand-by agreement with the IMF and EU candidate status will influence the obstacles to FDI we identified in chapter three. We also look in detail at how EU enlargement as whole will affect Turkey's competitive position as an investment location.

4.2. The IMF agreement

Turkish politicians are expecting the three-year $4 billion IMF stand-by agreement to make Turkey a significant centre of gravity for foreign capital. Turkish Economic Minister, Recep Onal, anticipates that once the government's determination over structural transformation is clearly understood and early positive results of the disinflation program are revealed, there will be a major leap in foreign capital flows (Xinhua News Agency, 2000).

At the cornerstone of the $4 billion IMF agreement is completing the privatisation of all state economic enterprises by 2001 (EIU, 2000) and reducing inflation to single digits by 2002.[******] The programme has got off to a good start. During the first four months of 2000, Turkey sold off $5.3 billion in state companies and operating licenses, exceeding the total privatisation of the past 17 years (KEW 12-18 Apr 2000). Inflation is also falling, although not by enough to reduce inflation to the forecast 25% by the end of 2000. There is widespread support and commitment for structural reform – in large part because it is

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also producing new models for the world market solely in Turkey. Toyota and Hyundai appear to be in the process of re-organising their Turkish ventures as major export platforms for the EMEA market. The IMF agreement and prospects of EU membership were likely to be decisive in these new investment decisions.

[******] The IMF agreement also involved new legislation that allows foreign investors to seek international arbitration in disputes over contracts involving the state. This has been one of the biggest obstacles to financing much needed energy and other infrastructure projects, and should encourage FDI inflows (EIU, 1999).

seen as Turkey's last chance to become a normally functioning market economy and to join the EU.

In chapter two we argued that low levels of privatisation-related FDI was the major factor explaining Turkey's under-performance in attracting FDI relative to the CEECs taken as group, and in chapter three we found that chronic inflation has been a major obstacle to competing for inward investment. The structural policies being implemented under the auspices of the IMF, if successful, are likely to remove two of the major obstacles to FDI. The interdependent relationship between privatisation, inflation and FDI is likely to lead additional multiplier effects on FDI in Turkey. Under the IMF agreement, privatisation receipts are being used to repay state debt, in order to reduce inflation. Privatisation itself will lead to direct FDI inflows as foreign investors take strategic stakes in state owned enterprises and the reduction in inflation will greatly improve the economic environment for investors, attracting additional independent FDI. The reduction in debt will also improve Turkey's credit ratings and the risk premium attached to investing in Turkey.

Furthermore, "a strong privatisation programme sends an important signal to the investor community, that the government is willing to support private sector development and remove impediments and restrictions on foreign involvement" (IFC, 1997: 43), which has a strong effect on the decision making process of foreign investors (Sader, 1995: V). This is the experience of countries like Hungary (Kaminski and Riboud, 1999) and in Poland the reduction in debt following deals with international creditors on external debt and financing also appears to have led to a sharp increase in FDI due to a change in perceptions (Orlowski and Szczepanska-Maciejuk, 1998).

If the Turkish government shows the necessary political commitment to relinquish strategic state control in a large number of state-owned enterprises,[†††††] then the IMF programme should lay the foundations for a rapid increase in FDI if the government uses this opportunity to promote wider FDI in Turkey.

4.3. EU enlargement

According to the EIU (2000), "Turkey's acceptance as an EU candidate should boost confidence, and will attract investment." However, only around 10% of our interview respondents saw the prospect of EU membership as one of Turkey's key strengths as an FDI location, while almost 30% of respondents cited not joining the EU as a key threat to Turkey's position (see SWOT analysis in appendix). As with creating a favourable FDI enabling and political-institutional environment, membership of the EU appears to be a pre-condition rather than an advantage if Turkey is to successfully compete for inward investment.

There are two key reasons why Turkey needs to join the EU as soon as possible if it is to become a centre of gravity for inward investment. First, the CEECs that join the EU first are likely to further divert FDI away from Turkey. Second, Turkish products cannot compete on a level playing field unless Turkey is a member of the EU or Single European Market.

[†††††] This must be through a fair and transparent process, not lengthened by bureaucratic procedures and indecisiveness (Megyery and Sader, 1997).

4.3.1.The impact of the CEECs joining the EU before Turkey

According to Eurostat (1997: 39), "it is clear that European companies have a tendency to respond to globalisation pressures by enhancing the division of labour through FDI within the EU rather than to third countries." Membership of the EU therefore makes a country more attractive for FDI from other EU countries. This argument has empirical support in the case of Ireland, Portugal and Spain. For example, Thomsen and Woolcock (1993) show that Ireland's share of US FDI doubled in first five years following membership and after Portugal joined the EC in 1986, FDI doubled every year 1987-1989. Spain experienced a similar increase in FDI following membership.

Membership of the EU brings access to markets, greater policy certainty, increased growth prospects and stability, access to structural funds, and membership of the Single European Market and the Euro, as well as a change in perceptions with the new member now psychologically part of "Europe."

Brenton (1999) demonstrates that the candidate countries themselves are their own principal competitors. Together with the EU being the most important export market for all of the candidate countries, "the impact of the next enlargement may be felt most heavily in those CEECs not included and in Mediterranean countries, such as Turkey" (Brenton, 1999: 75).

JETRO (2000) states that "leading US and European firms in fields such as auto/auto parts, finance, communications, aviation and energy are rushing to enhance their market position in the region, and FDI flows are expected to continue to grow in 2000." But this is only the case in countries where membership of the EU is a "distinct possibility." Hence, Kaminski and Riboud (1999) and Orlowski and Szczepanska-Maciejuk (1998) argue that the prospects of EU membership have already increased FDI in Hungary and Poland.

Differentiating between fast- and slow-track candidates in accession is therefore likely to divert trade and investment away from Turkey and those CEECs that are less advanced in their negotiations. The slow track countries will also be disadvantaged from their exclusion from structural funds that can be used to improve infrastructure and the business environment in the first wave members (Brenton, 1999).

In our interviews, three-quarters of respondents thought that the prospects of the CEECs joining the EU before Turkey will have at least a "significant" impact on FDI in Turkey, while one-third of respondents thought that joining the EU was important "to a great extent" for attracting FDI to Turkey. Turkey is going to find it harder to compete for FDI as it is excluded from the first wave of new members.

4.3.2. The impact of Turkey not being a member of the Single Market

While Turkey has a customs union with the EU, our research strongly suggests that this is not a substitute for being a member of Single European Market when it comes to attracting FDI. In our interviews, 45% of respondents thought that EU membership will have a major impact on access to markets, perceptions and image, and macro-economic stability in Turkey.

The frequency which respondents cited access to markets is surprising, given the customs union between Turkey and the EU. In fact, only one respondent said that membership of the EU would not lead to greater access to markets because of the pre-existing customs union. There are two key reasons why the customs union is not a substitute for joining the EU and the Single European Market:

- **The customs union has quotas:** Textiles are subject to quotas and the customs union excludes agriculture. Textiles are Turkey's main export sector and Turkey is the largest exporter to the EU. Turkey's textiles industry currently enjoys less protection than the EU's (EIU, 2000: 44).##### In agriculture, Turkey is one of the few countries in the world that is self-sufficient, and Turkey is the world's biggest producer of several commodities. The GAP project will dramatically increase Turkey's agriculture output, but Turkey will face quota restrictions when exporting to the EU.
- **The customs union has not prevented the use non-tariff barriers (NTBs).** This is a significant obstacle to Turkey competing in the EU in goods where it has a comparative advantage. According to Balasubramanyam (1996: 128), Turkey is reported to be cited in more anti-dumping cases by the EU than most other countries. A case in point is the European Commission's "Notice of initiation of anti-dumping proceedings" lodged in June 2000 concerning colour television receivers originating in or exported from Turkey – a sector which has been one of the major success stories of the customs union for Turkey.§§§§§§ The EU also applies local content requirements against Turkey. When Turkey was negotiating to join the customs union, the EC endorsed the view that Japanese transplants in Turkey do not have Turkey as their country of origin and requested Turkey not to export Japanese cars (Duna and Kutay, 1996: 176-177). In the end, Japanese automotive companies producing in Turkey had to have a 60% EU local content for cars to be exported to the EU

The EU similarly applies NTBs to the CEECs. For example, in 1995 2% of Polish imports to the EU were subject to anti-dumping duties or investigation (CEPS, 1998: 6). The OECD (1995) estimates that the costs of responding to anti-dumping duties in the CEECs are up to 10% of a firm's annual export revenues (cited in CEPS, 1998: 6). Association agreements with the CEECs also require 60% domestic content for printed circuit boards and automotive sectors products to enter the EU (Moran, 1999: 79). This has meant that auto plants in the CEECs have had to import high cost EU steel preventing utilisation of Hungarian, Polish or Turkish steel (Moran, 1999: 107-8).

Anti-dumping duties and rules of origin have therefore skewed "trade and investment patterns away from what international comparative advantage would otherwise predict" (Moran, 1999: 8). We recommend that Turkey and second wave applicants meet the requirements and negotiate to gain membership of the Single European Market, or at least

In July 2000 the EU decided to lift quotas imposed on Turkish textile imports between 2002 and 2005.

§§§§§§ Turkey's major producer, Vestel, increased its sales by 1000% between 1994 and 1998 and increased its share of the highly competitive European television market from less than 1% to 13%. White goods is another major success story: one in ten domestic appliances sold in the UK are made in Turkey, primarily by Arcelik.

provisions to avoid anti-dumping duties. This will become all the more urgent when the first wave of CEECs join the EU. As Brenton (1999) points out, the new members may themselves instigate anti-dumping duties against Turkey and other candidate countries.

4.4. Conclusion and policy recommendations

Our discussion of the IMF agreement and EU enlargement suggests that while Turkey is already addressing some of the key obstacles to inward investment, further action is urgently needed.

The $4 billion IMF agreement, if successful, will lead to privatisation and foreign involvement in many of Turkey strategic assets, which should send a positive message to other potential investors that Turkey is entering into a new era of greater policy certainty and less political interference in business. Equally as important is the dis-inflation aspect of the IMF agreement. Reducing inflation to single digit levels is a crucial pre-condition for attracting FDI.

While our research has found EU membership to be vital to Turkey's competitive position as an inward investment location, candidate status has also led to a greater scrutiny of Turkey's internal affairs, highlighting issues such as human rights, regional inequalities, and the conflict in the South East. This is likely to have a negative impact on FDI in the short term, but should provide a powerful impetus for change in the longer term. Turkey's candidate status also generates greater comparison with the CEECs. While our empirical research in chapter two demonstrated Turkey's underlying economic competitive strength, much of the comparison between Turkey and the EU is likely to continue to be along the political dimension. At present, with all the candidate countries except Turkey having met the Copenhagen criteria for starting EU accession negotiations, there is definitely a perception that Turkey will be the last to join the EU.

It is almost certain that the leading CEECs will join the EU before Turkey, and our research has found that this will have a major impact on Turkey's ability to compete for FDI. In fact, we found that not joining the EU and competition from the CEECs were two of the key threats facing Turkey position for attracting FDI (see SWOT analysis in appendix). Other research has also shown that competition within the region for inward investment is intensifying (Oman, 2000; JETRO, 2000; Balasubramanyam, 1996). Membership of the EU is vital for access to markets and funding, economic growth and stability, political stability, policy convergence, and for changing perceptions. We recommend that Turkey takes the necessary steps to meet the Copenhagen criteria as quickly as possible and negotiates for membership of the Single European Market to ensure a level playing field with the leading CEECs that join the EU first.

Turkey offers huge opportunities for inward investors, not least because of its large, dynamic economy, quality labour force, and position at the centre of a growing $1.5 trillion dollar regional economy. The IMF agreement and EU membership promise to remove many of the obstacles to inward investment in Turkey, in particular relating to minimal privatisation, chronic inflation, and obstacles to EU market access.

However, to benefit from its underlying strength as a location for FDI our research suggests that Turkey needs to develop far more effective investment promotion to respond

to poor image and brand awareness and lack of information on what Turkey has to offer.[*******] As one of our interview respondents commented: "If Turkey does not get its act together and offer a more coherent package and better promotion it will miss real opportunities."

Turkey's leading competitors for inward investment are developing increasingly sophisticated investment promotion strategies, which are not only helping them to "win" new FDI but are also creating dynamic benefits for their economies. For example, CzechInvest, the investment agency for the Czech Republic, has quickly established high brand awareness and a reputation as a professional agency. The agency has a clear targeted strategy and is investing in initiatives to link foreign investors with domestic suppliers and to promote the upgrading for foreign facilities over time. We therefore recommend a detailed review of the organisation and strategy of investment promotion in Turkey.[††††††]

Table 21 summarises our key policy recommendations for increasing FDI in Turkey and maximising the benefits for Turkey's economic development.

[*******] As the SWOT analysis in the Appendix indicates, Turkey also needs to broker better political and economic ties with neighbouring countries if it is to emerge as a major regional production and financial centre.

[††††††] For a detailed discussion of investment promotion see Loewendahl (2000); Young et al (1994); Wint (1993) and Wells and Wint (1991). See Loewendahl (2001) and Spar (1998) for how agencies facilitate FDI projects.

Table 21: Policy recommendations for increasing FDI in Turkey

Short term (1 year)	Medium term (2-4 years)	Long term (5-10 years)
Economic factors • Reduce inflation to single digits • Strategy of for developing IT&T infrastructure • Strategy for brining education to EU levels • Strategy for supporting R&D and innovation *Enabling Environment* • Complete major privatisation • Review of all investment promotion activities and develop a new strategy • Secure funding for new investment promotion activities *Political-Institutional factors* • Faster progress in meeting the Copenhagen criteria so EU accession negotiations can begin • Complete reforms needed to join the Single Market, especially competition law • Develop strategy to deal with institutional and political obstacles to FDI (e.g. bureaucracy, attitudes)	*Economic factors* • Ensure Turkey has a world class IT&T infrastructure • Increase education levels for all segments of society • Expand internet availability to all of population • Support for innovation, entrepreneurs and SMEs • Maintain low inflation *Enabling Environment* • Establish a new or expanded investment promotion agency • Cut investment incentives • Integrate investment promotion with economic development policy • Develop a network of regional agencies for FDI and economic development *Political-Institutional factors* • Remove obstacles to FDI (attitudes, corruption, judiciary, bureaucracy, etc) • Develop high quality intellectual property rights • Strategy for accessing and using EU structural funds	*Economic factors* • Support transition to a knowledge-based economy *Enabling Environment* • Develop a recognised brand image of Turkey, which differentiates Turkey's 'offer' to investors at the national and regional levels • Develop strong partnership between regions in Turkey and other EU regions for attracting FDI and for economic development • New promotion campaign for a Turkey 'in' the EU • Promote Turkey as a regional economic centre for Southern European, Balkans, Central Asia, Middle East and North Africa for strategic activities *Political-Institutional factors* • Join European Union • Aim for a marked improvement in regional relations, especially with middle east

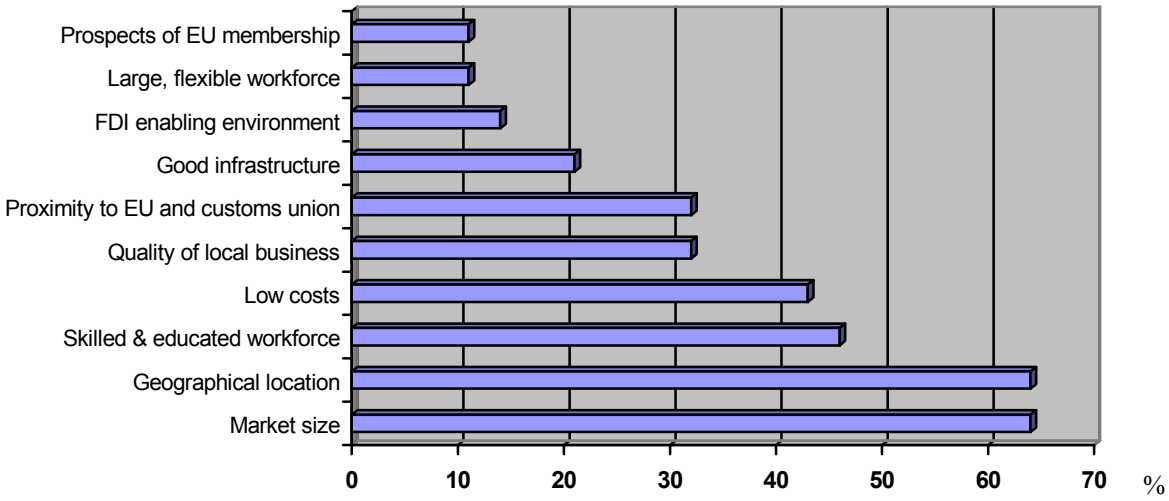
With the link between efficiency, market and asset seeking FDI increasing in importance in corporate location strategies, Turkey will continue to lose major opportunities to attract inward investment unless it takes urgent steps to reform its political-institutional environment and improve its investment promotion activities and image. While Turkey has one of the most dynamic markets in Europe for "new economy" activities, Turkey must also develop a strategy to increase its location advantages for asset-seeking FDI, through much greater support for its technological infrastructure and continued progress in its telecommunications and Internet infrastructure.

Attracting FDI cannot be considered in isolation from broader economic and political developments in Turkey. Economic stability, policy certainty and EU membership are pre-conditions for attracting significant investment into Turkey, but effective investment promotion and product development policies to develop the technological and human infrastructure are vital to successfully compete for and benefit from inward investment in the medium to long term.

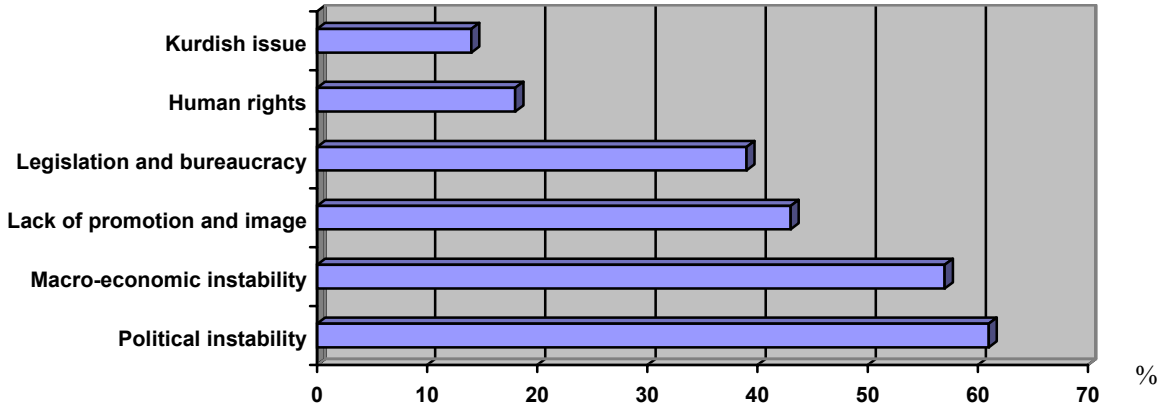
Appendix
SWOT Analysis

A SWOT analysis evaluates the strengths, weaknesses, opportunities and threats facing an organisation or a location. It can be used to facilitate strategy development. The below figures outline a SWOT analysis for Turkey as an investment location, based on our interview results. We evaluate the sectoral opportunities.

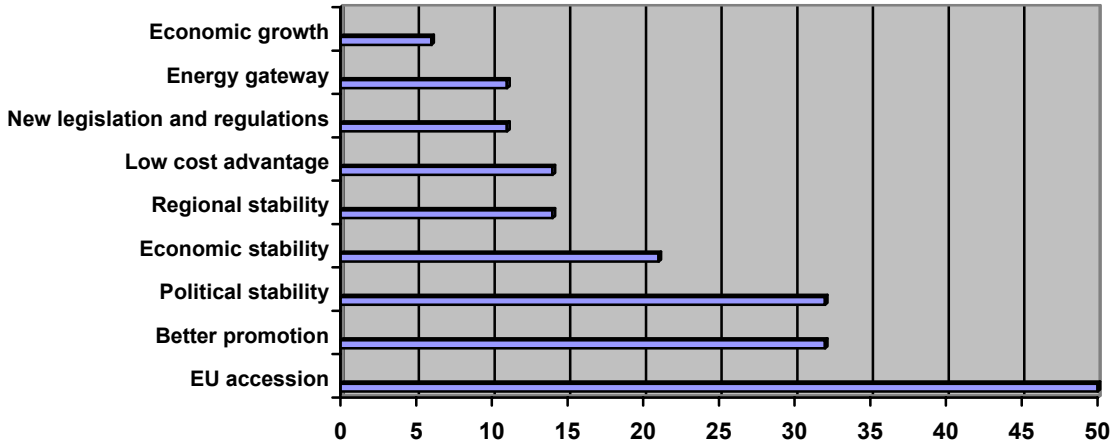
Key strengths of Turkey as an investment location
(% of respondents citing factor)



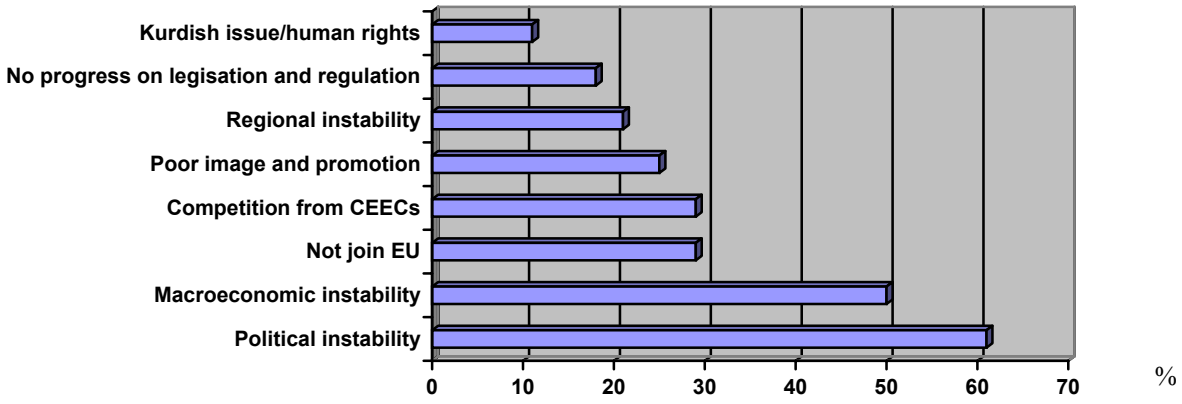
Key weaknesses of Turkey as an investment location
(% of respondents citing factor)



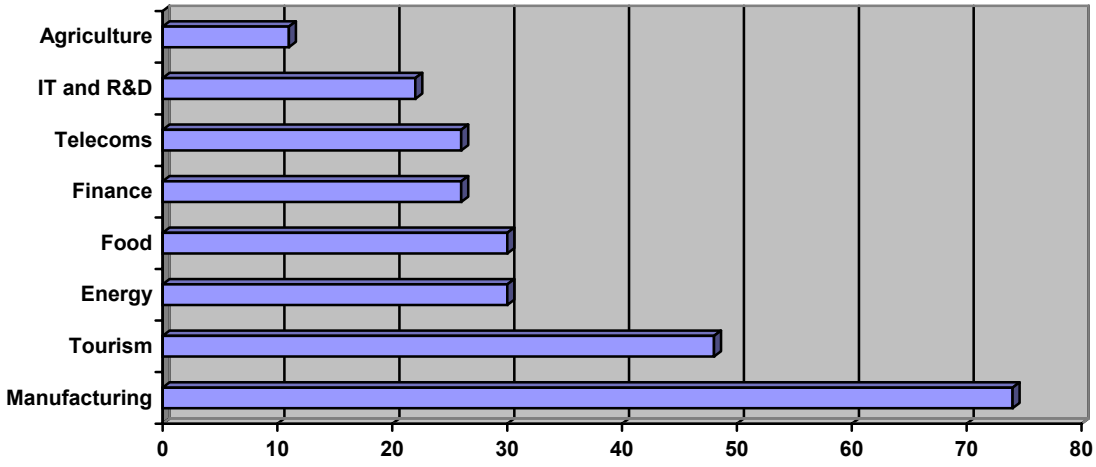
Key opportunities for increasing FDI in Turkey (% of respondents citing factors)



Key threats for Turkey's position as inward investment location (% of respondents citing factor)



Key sectors in which Turkey is in a strong competitive position to attract FDI (% of respondents citing factor)



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